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C O N F I D E N T I A L SECTION 01 OF 02 CHISINAU 000171

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SUBJECT: MOLDOVA: CHISINAU CAUGHT IN A COMMUNIST TRAP

REF: 07 CHISINAU 1520

Classified By: Ambassador Michael D. Kirby for reasons 1.4(b) and (d)

11. (C) SUMMARY: The opposition-controlled Chisinau municipal government is struggling with the decision of its Communist Party (PCRM) predecessor to increase and subsidize heating tariffs for all residents of the capital city. Although the current Chisinau city council attempted to cancel these measures, the PCRM controlled judiciary delivered a series of unusually swift court decisions against the municipal government. Chisinau was ordered to pay Termocom, the capital's heating company, Moldovan Lei 149 million (about USD 13 million) for heating debts. The IMF has raised concerns about Chisinau's mounting debts and implications for Moldova's current lending program, which sets a tight fiscal belt for 2008. With the heating season ending in seven weeks, Chisinau's municipal leadership hopes to survive short-term, while increasing tariffs and implementing subsidies prior to next year's heating season. We have no doubt that the PCRM central government will continue to be an obstacle to any solution. END SUMMARY.

ENGAGING WITH CITY HALL AND THE INTERNATIONAL COMMUNITY

12. (C) On February 19, the Ambassador hosted a luncheon with Chisinau Mayor Chirtoaca, City Council President Mihail Ghimpu (the mayor's uncle and Liberal Party leader), and the representatives of the EU presidency, EC, IMF, World Bank and UNDP in Moldova, to discuss Chisinau's legal battles with Termocom and the need to raise heating tariffs. The luncheon was organized in response to Ambassador's February 15 meeting with IMF Resident Representative Johan Mathisen, who noted the IMF's concern with Chisinau's mounting debts and the impact on Moldova's compliance with current lending program conditions, including a total (national and local) budget deficit cap of USD 25.5 million for 2008.

HEATING, TARIFFS AND DEBTS

13. (U) Centralized heating in Chisinau is provided by Termocom, which is owned by the municipality of Chisinau (70%) and private investors (30%), and serves 80% of the population in the capital city's mostly Soviet-era apartment blocks. Since 2001, the company has been in bankruptcy and under the control of the courts and a council of creditors, which include state-owned power companies and the partially state-owned MoldovaGaz. According to Moldovan law, the Chisinau municipal government, not the National Agency for Energy Regulation (ANRE), has the authority to set heating tariffs for Chisinau. In April 2007, shortly before the June elections, the then PCRM-controlled Chisinau municipal government decided to increase heating tariffs from Moldovan Lei (MDL) 233 per gigacalorie (gcal) to MDL 540/gcal.

14. (C) The increase was warranted as costs have risen considerably, yet the heating tariff in Chisinau had not been adjusted since 2000. However, in a populist pre-election move, the PCRM-controlled municipal council also agreed to subsidize the tariff. However, it also agreed to pay the subsidy bill in September 2007 following the local elections.

The difference between the old and new rates (about MDL 307/gcal) for all residents of Chisinau (excluding commercial enterprises) represented a significant burden on city finances. Faced with mounting deficits, on December 4, the current Chisinau municipal government voted to rescind the tariff increase, returning to the MDL 233/gcal tariff. After a series of judicial defeats, which Chirtoaca linked to the PCRM's influence over the judiciary, Chisinau was ordered to reinstate the MDL 540/gcal tariff and pay Termocom MDL 149 million for debts owed since December. Previously, Chisinau had partially paid for debts from April-November 2007, with a court ruling that the municipal government owed Termocom MDL 100 million and transferring the funds from the city's accounts. If a similar measure is taken to enforce the current judgment, the city's accounts will be drained, leaving only about MDL 14 million. Unless the municipal government can negotiate a payment agreement with Termocom, the city will be unable to pay salaries and operating costs.

CHISINAU'S PLAN FOR MOVING FORWARD

15. (C) Chirtoaca acknowledged that unless the Chisinau municipal government raised tariffs, debts generated by the subsidy would break the city's budget. He estimated the cost of the subsidy at MDL 300 million for 2007 and, if unchanged, at MDL 500 million for 2008 (out of a total budget of MDL 1.6 billion). Chirtoaca noted that this problem had been caused

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by his PCRM predecessors, but acknowledged that it would not simply go away. His challenge was how to solve the issue without losing political capital and giving the central government the opportunity to discredit the opposition for its inability to manage the city's finances.

16. (C) Chirtoaca and Ghimpu outlined their views on how to move forward. First, Chirtoaca noted, he would determine the real cost of heating, taking into consideration Termocom's input costs and the results of an audit of the company's finances. He added that previous PCRM control of Chisinau had led to murky business practices at Termocom. With this cost information, he would inform the public and the municipal government would determine the real tariff, setting a politically and economically viable consumer tariff with a targeted subsidy mechanism. If the city needed additional resources, Chirtoaca noted, he was willing (as a last resort) to sell municipally owned real estate.

17. (C) Ghimpu preferred to focus on the 2008-09 heating season, noting that the central government would do everything possible to discredit the opposition's management of Chisinau. He believed that politically the municipal government was obligated to provide consumer subsidies. He also worried that the central government, acting through Termocom and using the courts, would force another price increase to further squeeze the city's finances. Ghimpu noted that state-owned energy assets are known sources of financial support for the PCRM. Ghimpu ultimately acknowledged the need to increase tariffs, but was not as committed as Chirtoaca.

COMMENT

18. (C) We believe that our meeting will increase the Chisinau municipal government's sense of urgency about resolving the heating tariff problem. Chirtoaca understands that the PCRM central government wants him to fail and will continue to be an obstacle. However, his failure to increase tariffs and

negotiate a payment mechanism with Termocom in a timely manner has exacerbated the current problem. The IMF notes that Chirtoaca has been promising for months to increase the heating tariff for consumers but has yet to deliver. The Ambassador noted that the international community was ready to provide the political cover needed to implement a difficult tariff increase. In the short term, the Chisinau municipal government can generate the needed revenue by selling municipally owned land, however, this is not sustainable. Implementing a full cost recovery tariff and a targeted subsidy mechanism will be a true test of the young mayor's leadership and the opposition's ability to manage the capital city's finances. His uncle's very weak understanding of economics will complicate the mayor's task. END COMMENT.
KIRBY